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Supreme Court of the United States

OCTOBER TERM—1944

No. 536

SHEPARD BENJAMIN,

Petitioner,

against

JOSEPH JASPER, as Trustee in Bankruptcy of said SHEPARD BENJAMIN,

Respondent.

PETITION FOR CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SECOND CIRCUIT

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To the Honorable Chief Justice and Associate Justices of the Supreme Court of the United States.

The petition of Shepard Benjamin, bankrupt, prays that a writ of certiorari issue to review the order and decree of the Circuit Court of Appeals for the Second Circuit entered in the above case on the 5th day of August, 1944 (R. 72, 73) affirming an order of the District Court of the United States for the Eastern District of New York dated the 15th day of November, 1943 (R. 63). An order of the District Court reversed the order of the Referee in Bankruptcy dated the 10th day of June, 1943 (R. 57).

Opinions Below

The opinion of the Circuit Court of Appeals for the Second Circuit (R. 68 to 71, incl.) is not yet reported. The opinion was handed down by a divided Court, Circuit Judge Clark handing down a dissenting opinion.

In reversing the order of the Referee in Bankruptcy the District Judge rendered an opinion (R. 62).

The Referee, in granting the bankrupt his discharge, handed down a written decision (R. 54 to 56).

Jurisdiction

The decree of the Circuit Court of Appeals was entered on the 5th day of August, 1944 (R. 72, 73).

The jurisdiction of this Court is invoked under Section 24(c) of the Bankruptcy Act and under Section 240(a) of the Judicial Code as amended by the Act of February 13, 1925.

Questions Presented

In a proceeding in bankruptcy the petitioner applied for a discharge in bankruptcy. After specifications of objection to the bankrupt's application were filed the Referee dismissed the specifications and granted the discharge, holding that as to the bankrupt's failure to preserve books of account and records there was nothing in the testimony to establish such specification since the bankrupt, for the past six years, was employed as a salesman by the Borden Company and that the books of the several companies with which the bankrupt was associated were abandoned when these companies passed out of existence. The District Court reversed the Referee and denied the discharge of the bankrupt. The Circuit Court of Appeals, by a divided Court, affirmed the order of the District Court. The questions are:

1. Was the District Judge compelled, under Section 38 of the Bankruptcy Act and the applicable decisions, to accept the ruling of the Referee on the question of whether the bankrupt should be excused from preserving the books and records of the corporations because the same was justified under all of the circumstances, unless such ruling was clearly erroneous?

2. Does Section 14(b) of the Bankruptcy Act, which excuses a bankrupt from preserving the books of account or records from which his financial condition or business transactions might be ascertained when justified under all of the circumstances in the case, present a question of fact or law to be determined by the Trial Judge or Referee?

3. Was the Court below compelled to refer the case for further hearing before the Referee if it refused to accept the finding of the Referee in order not to deprive the petitioner of his rights under the due process of law clause of the Constitution?

Statement

The petitioner filed a voluntary petition in bankruptcy and in that proceeding made an application for a discharge from the scheduled liabilities. The petitioner, for the past six or seven years prior to the date of the bankruptcy, had been employed by the Borden Company as a salesman and for approximately ten or twelve years before that time had been engaged in the real estate business in the Borough of Brooklyn as the owner of stock in several corporations, to wit, the Caton Realty Corporation, the Shep Realty Corporation and the Avalon Realty Corporation. The respondent filed specifications of objection to the application for discharge. The objections were two in number and charged the petitioner with (1) having made and issued a false statement and (2) with the failure to preserve books of account or records of the corporations.

Hearings were held before the Referee and as a result thereof a decision was made by the Referee holding that the record does not establish that the bankrupt issued a false statement in January of 1928 and as to the failure to preserve books of account and records states that there was nothing in the testimony to establish that specification. The Referee accordingly made an order on June 10, 1943

dismissing the specifications and granting the discharge of the petitioner (R. 54 to 57, incl.).

The respondent filed a petition to review the said order of the Referee and the District Court, after hearing, handed down an opinion in which he agreed with the Referee as to the disposition of the first specification and as to the second specification held that the same should be sustained. On the 15th day of November, 1943, an order was entered by the District Court sustaining the specification charging the petitioner with failure to preserve books and records of account of himself or the corporations in which he was interested and providing that the discharge of the petitioner be denied (R. 62-64).

The petitioner filed a notice of appeal to the Circuit Court of Appeals and on the 7th day of July, 1944, the Circuit Court handed down a divided opinion which affirmed the order denying the petitioner his discharge and sustaining the second specification charging the petitioner with failure to preserve books and records of account for himself and for the corporations in which he was interested. The Circuit Judge in the dissenting opinion stated that the most that should be done in the interest of fairness is to send the case back for further hearing to the Referee because the Referee, believing the bankrupt's explanations, curtailed his testimony as to what the books might show and allowed no opportunity for explanation of the statement disclosing that the books were actually in existence long after their claimed abandonment (R. 71).

Reasons Relied On for the Allowance of Writ

1. The result of the decision of the United States Circuit Court for the Second Circuit would create a precedent of reviewing questions of fact even though the decision of the trier of fact is not clearly erroneous.

2. The decision of the United States Circuit Court of Appeals for the Second Circuit is contrary to the intent and purpose of Section 38 of the Bankruptcy Act which provides that the Referee shall grant, deny or revoke discharges and perform such other duties as are by the Acts of Congress relating to bankruptcy conferred on Courts of Bankruptcy.

3. The United States Circuit Court of Appeals has by its decision treated the finding of fact of the Referee merely as advisory to the District Court rather than as conclusive as to the finding of fact unless such findings were found to be clearly erroneous.

4. The United States Circuit Court of Appeals for the Second Circuit is divided in its decision as to whether a decision of the Referee on the finding of fact should be affirmed unless found to be clearly erroneous.

5. The decision of the United States Circuit Court of Appeals involves the interpretation of Section 38 and Section 14 (b) of the Bankruptcy Act, which is of vital importance and should be settled by this Court.

6. The decision of the Circuit Court of Appeals for the Second Circuit is contrary to the decision of the Ninth Circuit in *Hultman* v. *Tevis,* 82 F. (2d) 940; the Tenth Circuit in *Hedges* v. *Bushnell,* 106 F. (2d) 979; and the decision of the Second Circuit in *Gold* v. *John R. Blair Co.,* 142 F. (2d) 209.

7. The decision of the District Court and the United States Circuit Court of Appeals will deprive the petitioner of a full hearing, which is granted to the petitioner under the due process of law clause of the Constitution.

Specifications of Error to be Advanced

The Court below erred:

1. In holding that if the bankrupt has obligations from which he seeks to be relieved by a discharge he should have preserved records from which his financial situation might have been made plain, instead of leaving his oral testimony as to matters occurring many years before and an investigation for deeds and mortgages in the Register's office and for judgments and foreclosures in the County Clerk's office as the only means of information open to his creditors.

2. In holding by implication that Congress intended that the decision of a referee in a discharge proceeding in bankruptcy based upon an issue of fact is merely advisory to the District Court.

3. In failing to hold that the question of a right to a discharge is addressed to the sound discretion of the Referee with the exercise of which, except in cases of gross abuse or where the finding is clearly erroneous, the District Court should not interfere.

4. In failing to hold that the petitioner was not given an opportunity to make explanation with regard to the failure to preserve books and records due to the ruling of the Referee.

POINT A

The District Court and the Circuit Court of Appeals should not as a matter of law interfere with the finding of fact of a Referee in a discharge proceeding in bankruptcy unless such a finding is clearly erroneous.

The Referee in his decision stated that there is nothing in the testimony to establish the specification that the bankrupt failed to preserve books and records of account. The Referee went on to explain that the bankrupt was for the past six years employed by the Borden Company as a salesman and that the books of the several companies with which the bankrupt was associated were abandoned when these companies passed out of existence (R. 55, 56).

Section 38 of the Bankruptcy Act reads as follows:

> "Referees are hereby invested, subject always to a review by the judge, with jurisdiction to * * * (4) grant, deny, or revoke discharges; * * *."

Under this section the Referee conducts all proceedings relative to a discharge before him with the same power as a court in bankruptcy. The Referee hears all proceedings in connection with the application for discharge, makes a decision based thereon, and an order either denying or granting such discharge and sustaining or dismissing the specifications of objection.

Prior to the 1938 amendment specifications of objection to a bankrupt's discharge were referred to one of the Referees as Special Master for hearing and report. The report of the Special Master was advisory in nature and the District Court reviewed both the facts and the law with respect to the recommendations of the Special Master. Since the amendment in 1938 a completely new interpretation must be given to the decision of the Referee by

reason of Section 38 of the Bankruptcy Act as amended in 1938.

Under Section 38 the Referee is given the power, as a Court, to grant, deny or revoke discharges. The review which is given to the Judge under Section 38 is in the nature of an appeal and, being such, a decision of the Referee based upon a question of fact, cannot be set aside by the District Judge unless clearly erroneous. Consequently the Circuit Court of Appeals should not affirm a decision of the District Court when such decision reverses an order of a referee where the decision of the Referee is not clearly erroneous.

The District Judge states that it seemed to him that under the circumstances the failure to preserve the books would be the same as allowing the books to be destroyed. The circumstances refer to the facts. The District Judge did not say that the decision of the Referee was clearly erroneous.

The majority opinion of the Circuit Court of Appeals referred to the liabilities as listed in the schedules and pointed out what appeared to be a conflict in the testimony as given by the bankrupt as to the last time he had seen the books and records of the corporation. It is apparent that the Referee accepted the version of the bankrupt that these books and records were lost at the time of the dispossess some seven years before the bankruptcy. The Circuit Court did not say that this finding was clearly erroneous, as was necessary to enable it to hold that the decision of the Referee was properly reversed by the District Court. The petitioner's view of the law in this respect is recognized by the dissenting Judge wherein he states that

> "We have usually found it desirable to affirm a referee in granting a discharge based in the main upon his deductions as to the bankrupt's truthfulness in testifying and his not 'clearly erroneous' findings of facts."

In *Gold* v. *John L. Blair Co.* (C. C. A. 2), 142 F. (2d) 209, the Court, in a unanimous decision, stated as follows:

> "We cannot say that under the circumstances the decision of the referee was clearly erroneous and feel impelled to sustain his decision, as the district judge did, as a proper exercise of his discretion. Hultman v. Tevis, 9 Cir., 82 F. 2d 940; Hedges v. Bushnell, 10 Cir., 106 F. 2d 979."

Courts in the various circuits have held to the same effect.

> *Hedges* v. *Bushnell* (C. C. A. 10), 106 F. (2d) 979;
> *In re Horowitz* (C. C. A. 7), 92 F. (2d) 632;
> *Rosenberg* v. *Bloom* (C. C. A. 9), 99 F. (2d) 249;
> *Nix* v. *Sternberg* (C. C. A. 8), 38 F. (2d) 611.

The majority of the Circuit Court and the District Court in the case at bar have treated the decision of the Referee as though it were merely advisory. In his dissenting opinion Circuit Judge Clark preferred to follow the cases holding that the Circuit Court must affirm the Referee in granting a discharge based in the main upon his deductions as to the bankrupt's truthfulness in testifying unless such decision is clearly erroneous.

The decision of the Court below casts doubt upon the extent of the power or rights granted to a Referee under Section 38 of the Bankruptcy Act and the weight that the decision of the Referee should have upon a review before the District Judge. This question of the weight to be given to a Referee's decision on a matter which comes before him for decision as Referee rather than as Special Master not only affects issues raised by specifications of objection to a bankrupt's discharge but to all bankruptcy issues before a Referee for decision.

In order that there may be a uniformity of opinion and interpretation of the statute by the Circuit Courts for the various circuits it is entirely desirable that this Court pass upon that question and interpret it finally for the benefit of all circuits.

POINT B

The justification for the failure to preserve books and records was a question of fact to be determined by the Trial Judge and is not a question of law.

The statute involved, namely, Section 14(b) of the Bankruptcy Act, directs the Court to grant a discharge unless the bankrupt has:

> "* * * destroyed, mutilated, falsified, concealed, or failed to keep books of account, or records, from which his financial condition and business transactions might be ascertained; *unless the court deems such failure or acts to have been justified, under all the circumstances of the case.*" (Italics ours.)

The bankrupt in the case at bar was charged with the failure to preserve books at a time seven years prior to his bankruptcy when he did not contemplate bankruptcy. Testimony was adduced before the Referee with respect to the liabilities sought to be discharged, the bankrupt's interest in the corporations which maintained books and records of account, the time and manner in which the corporations were divested of their properties. References were made to the original foreclosure records, dispossess proceedings, etc., and the bankrupt's means of earning a livelihood for the past six or seven years as an employee of the Borden Company and the extent of his income during that time. The Referee, based upon the testimony, as a matter of fact rendered a decision that the bankrupt was entitled to his discharge, holding by implication that the failure to preserve the books and records was justified under all of the circumstances of the case. This was a finding of fact and not a conclusion of law.

The District Court and the majority of the Circuit Court treated the matter as though it were discretionary with the District Court to determine whether the failure to pre-

serve the books was justified under all of the circumstances. Since the amendment of 1938 gives the Referee the power to decide the question at issue rather than to hear and report to the Court, it could not have been intended by Congress to mean the District Court but rather that the Referee, for all purposes, is to be considered the Court in connection with determining whether the failure to preserve the books was justified under all circumstances of the case.

There is no question but that Congress intended that the decision of the Referee be final unless an aggrieved party files a petition to review, which would be in the nature of an appeal, and that the District Judge would then have the same right to review as an Appellate Court and that it would be limited strictly to the question of law and to the question of fact only where the decision of the Referee was clearly erroneous.

The decision of the District Court and the majority decision of the Circuit Court, in affirming the District Court, is an unwarranted interference with the decision of the Referee upon the question of fact, which Congress intended to leave to the discretion of the Referee under Sections 38 and 14(b) of the Bankruptcy Act. The majority opinion of the Circuit Court in effect stated that the bankrupt should not be granted his discharge because he was so careless in connection with the preservation of his records. That indicates a decision based upon a question of fact rather than of law.

In the case of *In re Sevcel*, 30 F. (2d) 102, the Court, at page 104, stated as follows:

> "His carelessness in that regard was just as evident when his business was prosperous as when it was poor, and it, taken together with the method adopted by him, negatives the charge of failure to keep books with intent to conceal his financial condition when his business became poor. In re Feldstein (C. C. A.), 115 F. 259; Taback v. Arai (C. C. A.), 21 F. (2d) 161; In re MacKenzie (D. C.), 132 F. 114; In re Idzall (D. C.), 96 F. 314."

In *In re Silverstein* (C. C. A. 9), 35 F. (2d) 497, the Court, at page 498, stated as follows:

> "The question before us is whether or not the court grossly abused its discretion in granting the discharge. As was stated by this court in Re Merritt:
>
> ' * * * The question of the right to a discharge is addressed to the sound discretion of the District Court, with the exercise of which, except in case of gross abuse, an appellate court will not interfere.' In re Merritt (Merritt v. Peters), 28 F. (2d) 679, and the following cases there cited: Woods v. Little (C. C. A.), 134 F. 229, 232; In re Lord (D. C.), 22 F. (2d) 301; Seigel v. Caretl (C. C. A.), 164 F. 691; In re Leslie (D. C.), 119 F. 406; Osborne v. Perkins (C. C. A.), 112 F. 127; Poff v. Adams, Payne & Gleaves (C. C. A.), 226 F. 187."

Under Sections 38 and 14(b) of the Bankruptcy Act Congress intended that the decision of the Referee is to be substituted for that of the Court and since that be the case the decision of the Referee should not be reversed by the District Court and the Circuit Court, unless the Court finds that the Referee has grossly abused his discretion in such finding. In the absence of such finding, in a decision based upon a question of fact, there should not have been any interference with the decision of the Referee.

Each case presents a different state of facts and it is for such reason that Congress intended that the decision of the Referee should not be set aside unless said decision is clearly erroneous or there was a gross abuse of discretion.

In *In re Weismann*, 1 Fed. Supp. 723, District Judge Patterson, in reviewing and confirming the report of the Special Master recommending the discharge, prior to the enactment of the 1938 amendment, stated as follows:

> "The report of the special master recommending that a discharge be granted to the bankrupt will be confirmed.
>
> "The first specification in opposition to discharge is that the bankrupt failed to keep books. Under Section

14b of the Bankruptcy Act, as amended by Act May 27, 1926, Section 6, 11 USCA Section 32 (b), the second ground for denying discharge is that the bankrupt 'failed to keep books of account, or records, from which his financial condition and business transactions might be ascertained; unless the court deem such failure * * * to have been justified, under all the circumstances of the case.' * * *

"Here the bankrupt had not been in business on his own account for many years. He had been employed by various corporations, in some of which he seems to have had a stock interest. The greater part, if not all, of his living had come from salary received. It would doubtless have been better business practice to have kept personal books of account showing receipts and expenditures, but we know that few men in such a situation actually do so. The failure of the bankrupt to keep books was therefore justified, and this specification has not been sustained."

Other cases in which courts have granted a discharge even though the bankrupt failed to preserve books and records or had destroyed books and records, depending upon the circumstances of the case, which were determined upon the facts in each particular case, are:

In re Block, 29 Fed. 110;
In re Milne, 40 Fed. 89;
In re Sperling, 72 F. (2d) 259;
In re Horowitz, 92 F. (2d) 632;
In re Morris Plan v. *Henderson* (C. C. A. 2), 131 Fed. 976;
In re Lepine, 4 Fed. 808.

POINT C

The constitutional right of the bankrupt in the case at bar is violated by a reversal without referring the matter back to the Referee for further evidence.

The majority opinion of the Circuit Court indicates that there was a discrepancy in the testimony of the bankrupt as to the time when the books of the corporation were last in existence. It seems that the Circuit Court put much stress on this discrepancy in the testimony in affirming the decision of the District Court. When the bankrupt was interrogated before the Referee on this matter the Referee stated as follows:

> "I will dismiss any specification which refers to the failure of keeping books and records during the period of time which he worked for seven years for the Borden Milk Company. I think such a period of time doesn't put any obligation on a bankrupt to maintain books and records where he has not been in business for such a period of time for himself."

This statement foreclosed any further explanation by the bankrupt as to the discrepancy in the testimony. If the Referee was in error in this respect then, as was said in the dissenting opinion:

> "* * * the most we should do in the interests of fairness is to send the case back for further hearing before the referee. For the referee, believing in the bankrupt's explanations, curtailed his testimony as to what the books might show and allowed no opportunity for explanation of the statement disclosing that the books were actually in existence long after their claimed abandonment. We should not allow a perhaps too favorable attitude of the trier to prove a trap when an appeal is taken from his decision."

Cases supporting the dissenting view are:

In re Slohm, 11 Fed. 928;
In re Markman, 41 Fed. 95;
In re Soroko, 34 Fed. 825;
In re Slutzkin, 40 Fed. 244;
In re Peters, 39 Fed. 38.

CONCLUSION

Wherefore it is respectfully submitted that this petition for a writ of certiorari should be granted to review the decree of the Court below.

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